



End of the First-Year Depreciation Incentives?

To: :

Re: First-Year Depreciation Incentives

As we all know, the recession caused Congress to dramatically increase tax incentives for businesses that expend amounts for capital equipment and certain building improvements. Congress expanded the long-standing Section 179 deduction to the point that it is currently at \$500,000 per year. And Congress similarly added an incentive in the form of 100% bonus depreciation for many new (rather than used) asset additions.

Congress extended these provisions into 2012, but did so at reduced amounts. With the economy gradually recovering and the budget pressures greater than ever, our expectation is that these 2012 limits signal the end of the large first-year deductions.

Overview of Bonus Depreciation

From 2008 through most of 2010, the bonus depreciation deduction was 50% of the cost of new assets. But for assets acquired and placed in service from September 9, 2010 through December 31, 2011, that deduction moves up to 100%. Congress has also extended the deduction into 2012, but at a lower 50% rate. Presently, the tax law does not extend bonus depreciation after December 31, 2012, and it appears that any extension is unlikely.

To qualify for either 100% or 50% bonus depreciation, the asset must have its original use commence with the taxpayer (i.e. it is new rather than used property), and must have a depreciable life of 20 years or less. Virtually all farm-use assets have a depreciable recovery period of 20 years or less, and accordingly all are eligible. Bonus depreciation has its greatest impact when applied to assets with a longer recovery period, such as machine sheds and shops with a 20-year depreciable life or drainage tile and culverts with a 15-year recovery period.

Overview of Section 179 Deduction

For most of the past decade, the Section 179 deduction was maximized at just over \$100,000. When the recession hit, Congress bumped the limit to \$250,000, but later increased the amount to \$500,000 for tax years beginning in 2010 and 2011. More recently, Congress indicated that for tax years beginning in 2012, the Section 179 deduction would drop back to \$125,000 (although inflation indexing is applied, and the actual number should be \$130,000 - \$135,000).

Not only will the Section 179 deduction shrink beginning in 2012, but fewer small businesses will have access to this write-off. During 2011, the deduction phases out if a taxpayer's eligible Section 179 asset purchases exceed \$2 million. But starting in 2012, the phase-out threshold is \$500,000 of asset additions.

The Section 179 deduction applies to both new and used asset additions. It applies to machinery and equipment, and special use or single purpose ag buildings such as bins, drying systems, and livestock barns. But it is not available for general purpose ag buildings such as machine sheds and shops, nor is it generally available to landlords who purchase or construct assets that are used by a tenant.

Quick Reference Chart

The following chart is a summary of the first-year depreciation incentives that are in the law through 2012, as well as the amounts that we expect to be applicable for 2013 and after. The latest legislation from Congress for 2012 seems to signal that these incentives are ending, and that the new norm for the Section 179 deduction would be \$125,000, although adjusted upward for annual inflation indexing.

Here is the summary chart:

First Year Depreciation Incentives

Calendar Year	Section 179 Limit ^A	Bonus Depr. (New assets only) ^C
2011	\$500,000	100%
2012	\$125,000 ^B	50%
2013 (estimated)	\$125,000 ^B	0%

^A Fiscal year taxpayers apply the Section 179 limit for the tax year beginning in 2011, 2012, or 2013.

^B The 2012 (and estimated 2013) Section 179 limits are inflation-indexed by reference to 2006.

^C All taxpayers, regardless of whether reporting on a calendar or fiscal tax year, apply the bonus depreciation (%) based on the calendar year the asset was acquired and placed in service.

If you have any questions regarding details on either the bonus depreciation deduction or Section 179, please contact us. And if you are planning on taking advantage of major purchases or improvements while these large allowances are still in the tax law, we recommend that you have a detailed depreciation projection prepared. These depreciation incentives can shelter a significant amount of income, but the eligibility rules can be tricky and it's important to have an accurate expectation of the deductions that will be coming your way.

Iowa Conformity

The State of Iowa has conformed to the Federal rules regarding Section 179 expensing of equipment for 2011. At this time the most recent legislation has not addressed the Section 179 limits for 2012 and beyond in Iowa. Iowa has not conformed to the bonus depreciation rules used at the Federal level for any year. If bonus depreciation is taken on a machine shed for Federal tax purposes, the same machine shed will be depreciated over 20 years for Iowa tax purposes, likely resulting in a disproportionate amount of Iowa taxable income compared to Federal taxable income.